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In the Supreme Court

of the United States

OCTOBER TERM, 1977

No. 77-1134

UNITED STATES OF AMERICA,

Appellee,

vs.

STATE OF MONTANA; DEPARTMENT OF REVENUE OF THE STATE OF MONTANA; and W. A. GROFF, as Director of Revenue of and for the State of Montana, and his successors in office,

Appellants.

On Appeal From the United States District Court for the District of Montana

Brief of the States and Territories of Virginia, Arizona, North Dakota, Alaska, Nebraska, Maryland, Hawaii, Nevada, Oregon, Alabama, Wyoming, Guam, Washington, Arkansas, Florida, West Virginia, Iowa, Idaho, New Mexico, Indiana, Puerto Rico, and Colorado as Amici Curiae in Support of Appellant's Jurisdictional Statement.

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I.

INTRODUCTORY STATEMENT

This brief is submitted by the signatory states as Amici Curiae in support of the Jurisdictional Statement in the above captioned case. This brief being sponsored and

filed by the aforementioned states; consent to its filing is not required. United States Supreme Court Rule 42(4).

II.
OPINIONS BELOW

The opinion of the 3-judge District Court for the District of Montana, Helena Division, is reported at 437 F. Supp. 354 (1977). Copies of that opinion, and the unreported opinion entered by said court on November 18, 1974, are appended to Appellants' Jurisdictional Statement as Appendix p. 5-35, and p. 65-75.

III.
INTEREST OF AMICI CURIAE

The interests of the states joined as Amici in this brief, revolve around what is believed to be the far reaching effects of this opinion as it relates to the question of state taxation of independent contractors performing work for the United States of America, (federal government).

The finding of the District Court majority, viz., that a constitutional infirmity exists in a tax levied upon independent contractors performing work for the federal government, because said tax generates income for the taxing state, clearly has serious consequences for states other than Montana. As the argument contained herein will demonstrate, such a position is not consistent with the previous decisions of this Court.

It is essential that this Court accept jurisdiction of this cause, and reaffirm constitutional standards previously established, so as to allow the legitimate and continued state taxation of independent contractors performing work for the federal government.

IV.
ARGUMENT

Several issues are raised in Appellants' Jurisdictional Statement which contain merit and which warrant this Court's review of this decision. However, of the issues raised, one is of singular importance not only to the State of Montana, but contains national implications of great importance to the Amici states as well. Therefore, this brief is limited solely to a discussion of that question.

THE ACT DOES NOT VIOLATE THE SUPREMACY CLAUSE OF THE UNITED STATES CONSTITUTION.

The tax in question is known as the Montana Contractors' Gross Receipts Tax, and is found in Chapter 35, Title 84, Revised Codes of Montana (1947). Basically, the tax is a levy of one percent of the gross receipts earned by public contractors within the State of Montana. The tax is levied on the contractor and not on the public agency. A public contractor is defined as any person performing a contract for the State of Montana or any other public body, including the federal government. The Act provides for a system of refunds and credits, whereby a contractor can receive a cash refund for personal property taxes, or a credit for any corporate income taxes. The tax is levied on all public contractors and makes no distinction, as to the state of incorporation or principal place of business. During the years of the operation of the tax, it has resulted in revenue being generated for the State of Montana equal to one-half of the amount of the tax collected — i.e. effective tax of ½ percent. [1]

[1] The Act has been questioned in the Supreme Court of the State of Montana on two different occasions by the federal government, acting through its contractor Peter Kiewit & Sons, Inc. For a discussion of the history of the Act and the legislative intent, *see Peter Kiewit & Sons Co. vs. State Board of Equalization*, 161 Mont. 140, 505 P.2d 102 (1973) and *Peter Kiewit & Sons Co. vs. Dept. of Revenue*, 166 Mont. 260, 531 P.2d 1327 (1975).

Several issues were raised by the federal government to support its contention regarding the invalidity of the tax. What will be discussed by the Amici in this brief, are the allegations, labeled as Supremacy Clause questions, that the Act discriminates against the government, its agencies and instrumentalities, and those with whom it deals. (Appellants' Appendix, page 92-94)

The district court, in finding that the Act violated the Supremacy Clause, based its decision on the fact that the state retained as general revenue one-half of one percent of the amount of the tax collected. The Court stated:

> "It is manifest from the above findings of fact that as between the State and the Government, the imposition of the G. R. Tax upon Contractors discriminates against the Government and in favor of the State. Although a public contractor for the State might add the G. R. Tax as a line item in his bid and thus increase the cost of construction, the State would receive as general revenue that portion of the G. R. Tax remaining after allowing credits and refunds. As indicated, that averages slightly less than 50 percent of the G. R. Tax. Contra, the Government is required to pay through increased bids by the imposition of the G. R. Tax and gets no return of the over plus of approximately 50 percent." (Appellants' Appendix, page 13.)

In support of its finding, the district court quoted from *Homestake-Sapin Partners vs. United States*, 375 F.2d 507, (10th Cir. 1967) citing from *Phillips Chemical Co. vs. Dumas Independent School District*, 361 U.S. 376, 80 S.Ct. 474, 4 L.Ed. 384 (1960), reiterating the well established doctrine, that a state must treat those who deal with the government as well as it treats those who deal with itself.

The district court found that because the tax levied on contractors performing public work generated tax revenue for the state and not the federal government, Montana was not complying with the "Golden Rule" of *Phillips Chemical*. The district court clearly misread and misapplied the *Phillips Chemical* rule and tested for equality of economic tax impact at the level of the sovereigns rather than at the level of those who deal with the sovereigns — i.e. the contractors. It is that crucial, fundamental and erroneous holding of this case which is so very disturbing to the Amici. This position is directly contrary to the previously established law in this area.

Beginning with the case of *James vs. Dravo Contracting Co.*, 302 U.S. 134, 58 S.Ct. 208, 82 L.Ed. 155, (1937), this Court upheld as being constitutional a "2%" tax imposed by a state upon the gross receipts of a contractor earned under contracts with the federal government. *See also, Silas Mason Co. vs. Tax Commission of Washington*, 302 U.S. 186, 58 S.Ct. 233, 82 L.Ed. 187 (1937), upholding the validity of an occupation tax applied to gross income received by individuals performing work for the federal government; *United States vs. Boyd*, 378 U.S. 39, 84 S.Ct. 1518, 12 L.Ed. 2d 713 (1964), upholding a tax levied by the State of Tennessee on property owned by the federal government, but used by independent contractors in the performance of federal contracts; *Alabama vs. King and Boozer*, 314 U.S. 1, 62 S.Ct. 43, 86 L.Ed. 3 (1941) upholding the validity of a sales tax levied upon contractors operating under a "cost plus a fixed fee" contract with the federal government;[2] *United States vs. City of Detroit*, 355 U.S. 466, 78 S.Ct. 474, 2 L.Ed. 2d 424 (1958), upholding the validity of a state tax levied on

[2] See also *U.S.A. and Hercules Inc. v. Forst*, ___ F.2d ___, (4th Cir. 1978), Case No. 77-1395 and 77-1722, decided January 23, 1978.

the lessee of property owned by the federal government. As stated in *United States vs. City of Detroit*, *supra*, at 469:

> "At the same time it is well settled that the Government's constitutional immunity does not shield private parties with whom it does business from state taxes imposed on them merely because part or all of the financial burden of the tax eventually falls on the government."

The cases make it clear that in order for a tax to be valid, it must (i) not have substantial economic impact on the federal government, (ii) not be levied directly on the federal government; and (iii) not be discriminatory. A review of the tax levied by the State of Montana herein indicates that it falls within these guidelines. It is a tax ¼ as large as the tax levied in the *Dravo* case, *supra* (½ of 1% as opposed to 2%); it is not direct as it is levied on the independent contractors and not on the federal government; and finally, it is not discriminatory as it is levied upon all contractors performing work for any public body, including the State of Montana and all counties, cities and special improvement districts, etc.

Yet the district court found this tax to be invalid on the grounds of discrimination, finding the state was not treating those who deal with the federal government as well as it treats those who deal with itself. (Appellants' Appendix, page 13.) The majority cited the case of *Phillips Chemical Co. vs. Dumas Independent School District*, *supra*, at 385, and the following test:

> "Accordingly, it does not seem too much to require that the state treat those who deal with the (federal government) as well as it treats those with whom it deals itself."

It is the position of the Amici that the district court has misapplied this "Golden Rule" test for discrimination. This tax is levied on all public contractors performing work for both the State of Montana (and its inferior governments) and the federal government. However, the district court found that because the tax generated revenue for the State of Montana and because this revenue is retained by the state, this results in discrimination under the Supremacy Clause. The fallacy of the argument lies in the fact that there is no way any state tax levied upon independent contractors performing work for the federal government could therefore be upheld.

Take for example the situation in the *Dravo* case, *supra*. In that instance, West Virginia levied a 2% tax on all contractors performing work in the state whether working for the State of West Virginia or the federal government. Under the reasoning of the majority opinion herein, a project costing $100,000 would in reality cost the State of West Virginia $98,000 (total cost minus 2% tax) or $2,000 less than the $100,000 project would cost the federal government. By following the majority's opinion that tax would be invalid under the Supremacy Clause, because the state retained as revenue the tax collected. Such a result cannot be allowed to stand.

Montana has treated all contractors dealing with public bodies in the same way, levying a tax on their gross receipts. A contractor performing work for the State of Montana (or any of its inferior governments), as opposed to a contractor performing work for the federal government, has been given no advantage. Rather, the "discrimination" that the majority opinion speaks of relates to the fact that the tax generated reduces the cost the state government ultimately has to pay. The test set

forth in the *Phillips Chemical* case, *supra*, does not make invalid a state tax levied on contractors performing work for the federal government merely because the monies end up in the coffers of the state treasury. Rather, it requires that if a tax is to be levied on a federal contractor, a like and equal tax must be levied on a state contractor.

The Amici are not alone in believing that the majority has misconstrued the *Phillips* test, and that if the opinion were left to stand, it could have a far reaching effect on the issue of inter-sovereign taxation. This thought was expressed very aptly by Judge Kilkenny in his dissent.

> "The reasoning of the majority *sub silentio* overrules this (Dravo) and other authority. In each of the above cases, the tax would apply equally to those doing work for the state government. Applying the reasoning of the majority, there is discrimination against the federal government because the otherwise legitimately collected tax (general state revenue) reduces the state's net cost, thereby allowing it to spend less than the federal government. Thus, under the guise of discrimination against the federal government, *any state tax could be traced backwards to defeat its own existence.* (Appellants' Appendix, page 28-29.)" (Emphasis added).

The Amici would also point out to the court the serious error the majority made in finding that the act also violated the Supremacy Clause because it discriminated against the government in favor of private contractors. (Appellants' Appendix page 15). What the majority did was use only Supremacy Clause standards in deciding a tax classification issue.

As the Jurisdictional Statement of the State of Montana indicates, it is necessary to also use Equal Protection rules when deciding tax classification questions. The tax in this case makes a distinction between public and

private contractors. The Montana Supreme Court in Kiewit No. 1, (Appendix page 105-123) found such a tax classification valid under the generally used Equal Protection standards. The Montana Supreme Court then went on to decide that the act did not violate the Supremacy Clause rules because it treated the State of Montana in the same way as the federal government.

What the majority has done in this case is to insert the United States into the status of a taxpayer, and then find under the Supremacy Clause that the government was not being treated as well as private contractors and rule the tax invalid. Initially, the government is not a taxpayer under the act, and it was incorrect for the majority to so hold. Also, such reasoning would invalidate any state tax, because whenever the government is looked on as a taxpayer, Supremacy Clause standards allow no other results anytime there is any classification between taxpayers.

A review of the recent opinion of this Court, *United States v. County of Fresno*, __ U.S. __, 97 S.Ct. __, 50 L.Ed. 2d 683, (1977) supports our position. The *Fresno* case involved the question of whether or not a state could levy a tax on employees of the federal government measured by the value of their possessorary interest in housing owned and supplied to them by the federal government. In holding the tax valid, this Court again reiterated the rule that taxes levied on those who deal with the federal government are valid as long as the tax is also imposed on similarly situated constituents of the state.

Here, the tax is levied on all similarly situated constituents, all the contractors doing work for any public agency. In making the determination of whether or not the tax classification is valid, it must be tested under the

traditional Equal Protection standards, as discussed in *Allied Stores v. Bowers*, 358 U.S. 522, 79 S.Ct. 437, 3 L.Ed. 2d 480 (1959), and not by Supremacy Clause standards alone. To allow the opinion of the majority to stand, which equates the federal government to the status of a taxpayer, will render all such state taxes invalid under Supremacy Clause reasoning.

CONCLUSION

This issue is of vital concern to the Amici and represents a question having nationwide impact in the field of inter-sovereign taxation. Therefore, we urge this Court to note probable jurisdiction in the present case and give plenary consideration to this and all other issues presented in Appellants' Jurisdictional Statement.

Respectfully submitted,

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